

No. 15,456

IN THE

United States Court of Appeals
For the Ninth Circuit

JOSEPH L. JOY, Trustee of the Estate
of Miller Scraper & Mfg. Co., Inc.,
Bankrupt,

Appellant,

vs.

BANK OF AMERICA NATIONAL TRUST AND
SAVINGS ASSOCIATION and CONSOLI-
DATED DISTRIBUTORS, INC., a corpora-
tion,

Appellees.

APPELLANT'S REPLY BRIEF
TO BRIEF OF APPELLEE
CONSOLIDATED DISTRIBUTORS, INC.

JAMES M. CONNERS,

989 Market Street, San Francisco 3, California,

LERRIGO, THUESEN, THOMPSON
& THOMPSON,

Security Bank Building, Fresno, California,

Attorneys for Appellant.

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Table of Authorities Cited

Cases

Pages

Chichester v. Commercial Credit Co., 37 C.A. 2d 439 (1940)	2, 3, 4, 5
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Codes

Civil Code:

Section 3014(1)(b)(ii)	3, 5
Section 3016.9	6
Section 3440	2, 7

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**APPELLANT'S REPLY BRIEF
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It seems clear, from a reading of all the briefs submitted in this case, that the legal issue presented in the case at Bar has never been decided by this Court. Neither the Appellee nor the Appellant has brought to the attention of the Court any case involving a similar factual situation to the one presented in the present proceedings. For this reason, Appellant believes that a thorough-going analysis of the factual

situation in the present case is necessary to determine the applicability of the existing law to resolve the issue presented.

For purposes of clarity, let it be remembered that Miller was the manufacturer-seller, Consolidated was the financed-purchaser and that the Bank financed the purchase of the scrapers by Consolidated from Miller. Arrangements for purchase by Consolidated were made under a Trust Receipt transaction. The mechanics of that transaction were thoroughly reviewed in previous Briefs and it has been decided by the Referee in Bankruptcy and affirmed by the District Court that, as between Miller and Consolidated, compliance with California Civil Code Section 3440 was required and was not met, and that, therefore, the sale between Miller and Consolidated was null and void. This decision results from the fact that there was no immediate or continued change of possession of the scrapers from Miller to Consolidated, as required by Section 3440 of the Civil Code. As a result of this decision by the District Court it was decreed that Consolidated had no right, title, or interest in the scrapers. The legal question is whether or not the Bank has a valid security interest in the scrapers as a result of its Trust Receipt transaction with Consolidated. To answer this question the following analysis is submitted.

Chichester v. Commercial Credit Co., 37 C.A. 2d 439 (1940), tells us that the security interest of the Bank as entruster under the Trust Receipt trans-

action can be derived from the financed-purchaser as Trustee or from any other person. This rule of law is set forth in Civil Code Section 3014 (1) (b) (ii). It is upon this rule of law set forth in the *Chichester* case and the Civil Code that the Appellees base their case. Let us examine this rule of law as it relates to the facts in the present case.

In all cases which have been brought to the attention of the Court involving Trust Receipt transactions, it was the financed-purchaser as Trustee under a Trust Receipt transaction with a financing company that became bankrupt; it was the Bankruptcy Trustee of the financed-purchaser, representing the creditors of the financed-purchaser, who claimed title to property as against another creditor of the financed-purchaser, to wit, the financing company. In none of the cases submitted has the finance company claimed a valid security interest against the creditors of the manufacturer-seller as represented by its Trustee in Bankruptcy. Appellant submits these distinctions are significant and control the outcome of the present litigation. It will be noted by the Court that in the *Chichester* case and other authorities submitted that the financed-purchaser obtained *actual possession* of the goods in which the financing company claimed a security interest under its Trust-Receipt transaction with the financed-purchaser. Appellees stress the point that in the *Chichester* case the financed-purchaser had neither title nor possession of the goods when he executed his Trust Receipt document giving the finance company a security interest in said goods. It

is agreed that it is not necessary, nor should it be, for the financed-purchaser to have title and possession before he executes a Trust-Receipt document, *since this is the method by which the financed-purchaser obtains title and possession to the goods*. The point is, that after the execution of the Trust-Receipt document, the financed-purchaser in the *Chichester* case, and in other authorities cited, *actually received possession of the goods from the manufacturer-seller*. The *Chichester* case and the other authorities cited by Appellee tell us that after the financed-purchaser has obtained possession of the goods, and then is rendered bankrupt, that his Trustee is Bankruptcy, representing his creditors, will not prevail as against his other creditor, the financing company. *This is by reason of the fact that the Trust Receipt transaction between the parties gave the financing company a valid security interest good as against all other creditors of the financed-purchaser*. In other words, as between creditors of the financed-purchaser the beneficiary of the Trust-Receipt document prevailed. Herein lies the distinction between the cases cited to the Court and the facts in the case at Bar.

As a result of the Trust-Receipt transaction between Consolidated and the Bank, Consolidated became indebted to the Bank. A debtor-creditor relationship then existed between Consolidated, as a financed-purchaser, and the Bank who financed the purchase for Consolidated. In the cases submitted by Appellees conflicting claims to the goods in the hands of the Bankrupt were presented by two sets of creditors

of the Bankrupt. In the present case, the conflicting claims to the goods are between the Bank, a creditor of the financed-purchaser, and the creditors of Miller, the manufacturer-seller, represented by the latter's Trustee in Bankruptcy, the Appellant. *The claims are not between two sets of creditors of the Bankrupt. There is no debtor-creditor relationship between Miller and the Bank as a result of the Trust Receipt transaction between the Bank and Consolidated.* The Bank is not seeking to establish a valid security interest against other creditors of Consolidated but against the creditors of Miller who is not indebted to the Bank. Therefore, different legal principles are applicable to each situation. The Bank by obtaining a Trust Receipt from Consolidated *protected itself against a claim to the goods by other creditors of Consolidated.* As between creditors of the same debtor, the beneficiary of a Trust-Receipt document is held to prevail and with this point of law, Appellant has no quarrel. It should be pointed out that it is exactly in this situation that arguments of Appellees based on the *Chichester* case and Civil Code, Section 3014 (1) (b) (ii) apply. The security interest of the entruster in this situation may properly be derived from the Trustee or from any other person *without endangering the entruster's security interest as against other creditors of the Trustee.*

The Trust-Receipt document, however, should not be held to establish a valid security interest in the goods for the Bank as against the claims of the creditors of Miller. Suppose a creditor of Consolidated

intending to loan money to Consolidated conducts a search to ascertain the outstanding indebtedness of the latter? The Statement of Trust Receipt Financing filed with the Secretary of State would warn this creditor and give him notice that Consolidated might be indebted to the Bank as a beneficiary under any outstanding Trust Receipts. As between the Bank and the searching creditor, the Bank, by reason of its Trust Receipt transaction with Consolidated, has established a valid security interest against the other creditors of Consolidated. For commercial convenience, the Trust Receipt law did away with the necessity for a change of possession *between the financed-purchaser and the financing company*. Should this same rule apply when the Bankrupt is not the debtor under the Trust-Receipt transaction, but rather the manufacturer-seller and supplier of the debtor? Appellant thinks not. Suppose a creditor of Miller, the manufacturer-seller, had made inquiry of the office of the Secretary of State to ascertain if Miller was named as Trustee in any Statement of Trust Receipt Financing filed pursuant to Civil Code, Section 3016.9, he would receive a negative reply from the Secretary of State, as Miller could not be a party to a Trust Receipt covering any of the scrapers because of the sales agreement entered into by it with Consolidated. (T.R. p. 191-213.) No creditor of Miller could have been put on notice of any outstanding lien under Trust Receipts in favor of the Bank on goods remaining in the possession of Miller, the manufacturer-seller. He would have no notice that a debtor-creditor rela-

tionship might exist between the Bank and Miller, the manufacturer-seller. He had no information that although a transfer of possession from the manufacturer-seller to Consolidated has not been effected, that nevertheless, the goods remaining in the possession of Miller, the manufacturer-seller, are encumbered with a lien in favor of the Bank. The reason why he has no knowledge of these things is simply because the Trust Receipt transaction, by its very nature, affects the rights and liabilities of Consolidated, the financed-purchaser, and *only* its creditors.

It seems clear then, that a Trust Receipt transaction is not designed for the protection of the creditors of the manufacturer-seller but rather for the creditors of the financed-purchaser. *Section 3440 of the Civil Code was designed to protect the creditors of the manufacturer-seller and it is the rights of these creditors of Miller, the Bankrupt, that are at issue.*

After an analysis of the facts in the case at Bar, it seems apparent that a condition precedent to a valid Trust Receipt transaction is compliance with Section 3440 of the Civil Code between Miller, the manufacturer-seller, and Consolidated, the financed-purchaser, required a change of possession between the parties.

It is the position of Appellant, *as to creditors of Miller*, that the validity of the security interest of the Bank was dependent upon an immediate and continued change of possession between Miller and Consolidated in compliance with Section 3440 of the Civil Code which the District Court ruled had not occurred.

Appellant respectfully submits (1) that the District Court erred in holding that the *invalid derivative security interest* of the Bank was effective as against the Bankruptcy Trustee of Miller, and (2) that this Honorable Court should reverse the *inconsistent* portion of the Order of the District Court from only which Appellant has appealed.

Dated, October 9, 1957.

Respectfully submitted,

JAMES M. CONNERS,
LERRIGO, THUESEN, THOMPSON
& THOMPSON,
Attorneys for Appellant.